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Tax News

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Whether or not there will be a further reduction in taxes in 1946 is problematical. H.R. 5293, called the "Incentive Income Tax Act of 1946" has been introduced in the House of Representatives. It has *NOT* passed any Committee or either house of Congress. While the bill has only been introduced, it is indicative of right thinking about Taxes by some one. Here are some of the provisions of the proposed law:

For years after December 31, 1945 — 25% on individuals and corporations alike on first \$5,000.00 net income, 5% increase on each \$5,000.00 to 50% on all incomes in excess of \$25,000.00.

Exemptions: \$2,500.00 for corporations, and married persons filing joint returns, and \$1,250.00 for single persons or those filing separate returns. Credit would be allowed on dividends received from domestic corporations by both individual and corporate taxpayers.

It will be worth watching the action, if any, taken by the House of Representatives, on H.R. 5293.

CITY OF LOS ANGELES SALES TAX

Visitors to the City of Los Angeles and its citizens will pay a sales tax of $\frac{1}{2}$ of 1% on purchases after May 11, 1946. The same exemptions apply as under the California State Sales Tax Law, except that the City of Los Angeles further exempts alcoholic beverages, including wine and beer. The tax applies only in the City of Los Angeles, not in any of the suburban cities. The additional exemption on alcoholic beverages will be an added accounting problem in many business houses subject to the new tax. The businesses having branch stores in the suburban districts and in the city will have to make changes in their overall accounting systems to compute the tax.

The Los Angeles metropolitan area is composed of numerous independent municipalities, the City of Los Angeles and unincorporated county areas. The Mayor of Los Angeles urged other metropolitan cities and the county to join him in his move for a city sales tax, but received no cooperation from these sources.

The first returns of the new tax will cover sales from May 11th to June 30th, and are due within 30 days. After July 1st,

taxpayers paying state sales tax monthly will remit to the city monthly. Those paying state sales tax quarterly will pay city tax on the same basis.

TRANSFeree'S LIABILITY FOR FEDERAL TAXES

On January 31, 1946, the Treasury Department, Internal Revenue Service of New Haven, Connecticut, sent a letter to stockholders of the Northwestern Telegraph Company, from which the following is quoted:

"You are advised that there will be assessed against you the amount of \$..... income tax, plus interest as provided by law, constituting your liability as transferee of assets of Northwestern Telegraph Company, . . . for unpaid income taxes for the taxable years ended December 31, 1939, 1940 and 1941, plus interest due—as shown on the statement attached." The attached statement showed the amount of income tax assessed against the company for the years 1939, 1940 and 1941. The stockholders' liability was limited to the amount of dividends received in those years. These dividends are described by the Government as "Assets Received".

This letter was startling and amazing to some stockholders while others were aware of the litigation started in 1924 by the Government to recover income taxes from Northwestern. However, all holders of the stock are facing a big tax bill to cover the judgment which the Government entered against the company on February 16, 1944.

The Northwestern Telegraph Company, contrary to appearances, is acting in good faith. On May 7th, 1881, this company leased its entire property to Western Union, the rental for which, was to be paid direct to the stockholders and bondholders, in the form of dividends and interest. This contract was entered into long before the Sixteenth Amendment authorized income taxes. The only property retained by Northwestern was 18 shares of its treasury stock, and an office was maintained for the transfer of stock and other routine matters only. Except for dividends paid on company-held treasury stock, all income from their property is paid directly to the stockholders.

The first suit brought by the Govern-

(Continued on Page 14)

the county, or for such other public works as are under the supervision of the county road commission.

Every domestic or foreign corporation doing business in Michigan, upon request by the Department of Revenue, must file with the department a list of its Michigan resident shareholders, containing the names, addresses and amount of its stock held by such shareholder, according to the last available records of the corporation.

The Department of Revenue will publish a list of corporations doing business in Michigan as well as a large number of other corporations, showing the par or contributed value of its stock. Supplements will be published from time to time as deemed necessary. Once having obtained the par or contributed value, the taxpayer may continue to use such value from year to year in the preparation of returns but shall change such values if corporate changes affect the capital structure of the corporation resulting in a different par or contributed value.

Contributed value of no-par stock of corporations shall be the average contribution of each such share to capital, paid-in surplus or other funds of the corporation, not including any earned surplus or deficits.

Stock acquired under the employees' stock purchase plan is taxable in the same manner as other stock unless held in trust, in which case it is taxable the same as other trust property. As soon as the stock is set aside for the employee and he receives dividends the stock is taxable to him.

Every corporation, domestic or foreign, doing business in the State of Michigan, is required to file with the Department of Revenue a copy of its return filed annually with the Michigan Corporation and Securities Commission, for the purpose of assisting the Department of Revenue in arriving at the percentage of the property of the corporation located outside of Michigan.

TAX NEWS — (continued from page 7)

ment to enforce payment of income tax by Northwestern was against Western Union, with Northwestern and its stockholders as co-defendants. The Government sought to collect from the latter taxes on the income of Northwestern for the years 1917 to 1922. A decision was rendered by the District Court, Southern District of New York in 1926. The Government lost in this case. Western Union had paid the rental to the stockholders in accordance with the lease agreements and had no property belonging to Northwestern.

The above decision was affirmed by the Circuit Court of Appeals, second Circuit in June, 1931. The Court held that Northwestern had no beneficial interest in the payments made to stockholders, and that such payments could not be reached by the Government.

In District Court, District of Connecticut, the Government sought a judgment against Northwestern Telegraph Company for income tax assessed against them for the years 1927, 1928, 1929, 1930. In January 1935, the Court denied the Government's claim on the basis that the income on the leased property was offset by a deduction for the same amount for interest on business indebtedness paid to the shareholders.

This decision was appealed to the Circuit Court of Appeals, Second Circuit, which on May 11, 1936 reversed the decision of the District Court, in favor of the Government. The court made the following statement "We do not think that the stockholders can avail themselves of a corporate organization to avoid the double tax, which is ordinarily imposed where income arises from the property of a corporation, and is paid to its stockholders, without subjecting themselves to such tax liabilities as may be inherent in the relation. The liability is because the property which belongs to whoever may be the stockholders' associates in corporate form, produces the income that passes to the recipients only as stockholders."

Northwestern's request for a review of the case in the United States Supreme Court was denied. Subsequently the Government secured judgments for income taxes for the years 1927 to 1941.

In March, 1945, the Government notified stockholders in New York, Connecticut and Vermont of proposed tax assessments for the years 1940 and 1941. Several stockholders filed petitions in the United States Tax Court. One case was tried in September 1945, and final briefs were filed in January 1946, but to date no decision has been made in the case. Other cases have been started to determine the liability of the stockholders as transferees, but it will take time to determine the outcome.

In the meantime, to avoid further interest the stockholders must pay the assessments. If decisions are rendered in favor of the stockholders, claims for refunds will be filed by those who have paid the Government. Northwestern is one of many corporations whose entire properties are leased to another corporation, the lessor paying the rental direct to the stockholders. Owners of this stock have a contingent liability for future assessments by the government.